

**REPORT OF THE AUDITOR-GENERAL TO THE KWAZULU-NATAL PROVINCIAL
LEGISLATURE AND THE COUNCIL ON GREATER KOKSTAD MUNICIPALITY
REPORT ON THE FINANCIAL STATEMENTS**

Introduction

1. I have audited the financial statements of the Greater Kokstad Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2012, the statement of financial performance, statement of changes in net assets and the cash flow statement for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting Officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Local Government: Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on the financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the municipality's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis for qualification

Property plant and equipment

6. The municipality utilised an expert to value infrastructure assets which subsequently increased the carrying value from R110,6 million (cost: R276 million) to R270,3 million (cost: R731,2 million) at year-end, an increase of R159,7 million (cost: R455,1 million) as disclosed in note 8 to financial statements. The opening carrying value of infrastructure assets was restated accordingly from R103,1 million to R283,5 million, an increase of R180,4 million. The input data and assumptions used by the expert to value the items of infrastructure assets could not be confirmed. Sufficient appropriate audit evidence could not be provided for audit purposes to substantiate that the expert's valuation methodology was appropriately and consistently applied. The municipality's records did not permit the performance of reasonable alternative audit procedures. Consequently, I was unable to confirm the valuation of infrastructure assets, as well as depreciation and accumulated depreciation.
7. The asset register included infrastructure assets with carrying values at year-end of R36,6 million (cost: R120,7 million), which did not include names or other uniquely identifying fields to allow me to determine the existence thereof. I was unable to perform any alternative procedures in this regard. Consequently, I could not confirm the existence of and rights to infrastructure assets.

Investment property

8. The municipality utilised an expert to value investment property which subsequently decreased the value by R4 million from R7,6 million to R3,6 million as disclosed in note 7 to the financial statements. Sufficient appropriate audit evidence could not be provided to substantiate the expert's basis for reducing the value of the investment property. Consequently, I could not obtain adequate audit assurance as to the valuation of investment property.

Qualified Opinion

9. In my opinion, except for the possible effects of the matters described in the Basis for qualified opinion paragraphs the financial statements present fairly, in all material respects, the financial position of the Greater Kokstad Municipality as at 30 June 2012, and its financial performance and cash flows for the year then ended in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

10. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

11. As disclosed in note 38 to the financial statements, the corresponding figures for 30 June 2011 have been restated as a result of errors discovered during 2012 in the financial statements of the Greater Kokstad Municipality at, and for the year ended, 30 June 2011.

Irregular expenditure

12. As disclosed in note 33 to the financial statements, irregular expenditure amounting to R11,273 million was incurred during the year, mainly as a result of contract awarded to suppliers in contravention of the Local Government: Municipal Supply Chain Management Regulations (GRN 868 of 30 May 2005) (Municipal SCM Regulations).

Unauthorised expenditure

13. As disclosed in note 42 to the financial statements, unauthorised expenditure amounting to R42,465 million was incurred by the municipality as a result of reduction in revenue based on the supplementary valuation roll, increase in salary costs and escalation in prices for electricity.

Additional matter

14. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited supplementary schedules

15. The supplementary information set out on pages ... to ... does not form part of the financial statements and is presented as additional information. I have not audited the schedules and, accordingly, I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

16. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

17. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages ... to ... of the annual report.
18. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury *Framework for managing programme performance information* (FMPPI).
19. The reliability of the information in respect of the selected objective is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).
20. The material findings are as follows:

Usefulness of information

Presentation

Measures taken to improve performance not disclosed

21. Improvement measures in the annual performance report for all planned targets not achieved were not disclosed, as required by section 46 of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA). This was due to inadequate internal policies and procedures over the processes pertaining to the reporting of performance information.

Consistency

Reported indicators not consistent with planned indicators

22. The MSA section 41(c) requires that the integrated development plan should form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total of 26% of reported indicators are not consistent with the indicators as per the service delivery budget implementation plan (SDBIP). This is due to the council's lack of understanding and oversight of the integrated development plan component with respect to the application of the principles of consistency in terms of the MSA and the Municipality Planning and Performance Management Regulations, 2001.

Reported targets not consistent with planned targets

23. The MSA section 41(c) requires that the integrated development plan should form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total 21% of reported targets are not consistent with the targets as per the service delivery budget implementation plan (SDBIP). This is due to the council's lack of understanding and oversight of the integrated development plan component with respect to the application of the principles of consistency in terms of the MSA and the Municipality Planning and Performance Management Regulations, 2001.

Compliance with laws and regulations

24. I performed procedures to obtain evidence that the municipality had complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA are as follows:

Annual financial statements

25. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of non-current assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected. The uncorrected material misstatements, however, resulted in the financial statements receiving a qualified audit opinion.

Procurement and contract management

26. Awards were made to providers whose directors are persons in service of other state institutions, in contravention of SCM regulation 44.

Asset management

27. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Expenditure management

28. The accounting officer did not take effective steps to prevent irregular expenditure and unauthorised expenditure, as required by section 62(1)(d) of the MFMA.

Internal control

29. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

30. The accounting officer did not exercise effective oversight responsibility to ensure that the municipality complies with laws and regulations and has an effective system of internal control over asset and performance management. Consequently actions were not taken to mitigate weaknesses to timeously respond to financial and compliance related risks.

Financial and performance management

31. Management did not perform monthly assets reconciliations to support complete, reliable and accurate financial reporting. Systems and controls were not designed in a manner to prevent, detect and address risks that impact on financial and performance, as well as compliance reporting.
32. Compliance with applicable laws and regulations was not monitored regularly. This resulted in material corrections in financial statements and reportable compliance related issues.

Pietermaritzburg

30 November 2012



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence